Supreme Court, U.S.
FILED
NOV 1 1993
OFFICE OF THE CLERK

No. 93-520

IN THE
Supreme Court of the United States
OCTOBER TERM, 1993

GEOFFREY, INC.,
Petitioner,

v.

SOUTH CAROLINA DEPARTMENT OF
REVENUE AND TAXATION,
Respondent.

On a Petition for a Writ of Certiorari to the Supreme Court of South Carolina

---

BRIEF OF AMICUS CURIAE TAX EXECUTIVES INSTITUTE, INC. IN SUPPORT OF PETITIONER

TIMOTHY J. MCCORMALLY
Counsel of Record
MARY L. FAHEY
TAX EXECUTIVES INSTITUTE, INC.
1001 Pennsylvania Avenue, N.W.
Suite 320
Washington, D.C. 20004-2505
(202) 638-5601
Counsel for Amicus Curiae
Tax Executives Institute, Inc.

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

BEST AVAILABLE COPY

TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	ii
INTEREST OF AMICUS CURIAE	1
SUMMARY OF ARGUMENT	2
ARGUMENT	6
CONCLUSION	20

TABLE OF AUTHORITIES

CASES: Page

Baldwin v. G.A.F. Seelig, Inc., 294 U.S. 511 (1935) 7-8, 16

Boston Stock Exch. v. State Tax Comm'n, 429 U.S. 318 (1977) 7

Burger King Corp. v. Rudzewicz, 471 U.S. 462 (1985) 16

Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977) 3, 8

Exxon Corp. v. Department of Revenue, 447 U.S. 207 (1980) 9

Freeman v. Hewit, 329 U.S. 249 (1946) 8

International Harvester Co. v. Department of Treasury, 322 U.S. 340 (1944) 9

International Shoe Co. v. Washington, 326 U.S. 310 (1945) 7, 16

Miller Bros. v. Maryland, 347 U.S. 340 (1954) 8

Milliken v. Meyer, 311 U.S. 457 (1940) 16

Mobil Oil Corp. v. Commissioner of Taxes, 445 U.S. 425 (1980) 9

National Bellas Hess, Inc. v. Department of Revenue, 386 U.S. 753 (1967) 3, 8, 10

National Geographic Society v. California Bd. of Equalization, 430 U.S. 551 (1977) 15

Quill Corp. v. North Dakota, 112 S. Ct. 1904 (1992) ..... *passim*

Runyon v. McCrary, 427 U.S. 160 (1976) 11

Shaffer v. Heitner, 433 U.S. 186 (1977) 17

Trinova Corp. v. Michigan Dep't of Treasury, 498 U.S. 358 (1991) 8-9

Tyler Pipe Industries, Inc. v. Washington State Dep't of Revenue, 483 U.S. 232 (1987) 10

Wisconsin v. J.C. Penney Co., 311 U.S. 435 (1940) 9

Wisconsin Dep't of Revenue v. William Wrigley, Jr., Co., 112 S. Ct. 2447 (1992) 2, 5, 7, 17-18

FEDERAL CONSTITUTIONAL PROVISIONS:

U.S. Const. art. I, § 8, cl. 3 7

U.S. Const. amend. XIV, § 1 7

TABLE OF AUTHORITIES—Continued

FEDERAL STATUTES: Page

Pub. L. No. 86-272, 73 Stat. 555 (codified at 15 U.S.C. § 381 (1988)) ..... *passim*

MISCELLANEOUS

CARROLL, LEWIS, THROUGH THE LOOKING GLASS (Signet Classic 1960) 15

Fahrenbach, Robert M., *DOR to Monitor* Geoffrey *Case, Intercompany Transactions*, 5 STATE TAX NOTES, July 26, 1993, at 300 19

Federation of Tax Administrators, *South Carolina High Court Applies* Quill *Decision*, 57 TAX ADMINISTRATORS NEWS 69 (July 1993) 19

HARTMAN, PAUL J., FEDERAL LIMITATIONS ON STATE AND LOCAL TAXATION (1981) 8

Peters, Jeffrey S., *Commentary: Income Tax Notes —Geoffrey Raises New Questions after* Quill, OHIO TAX SERV. 9-11 (Dec. 1992) 19

Townsend, William D., *Revenue Department Drafts Substantial Rewrite of Corporate Income Tax Rules*, 5 STATE TAX NOTES, July 5, 1993, at 7 19

BRIEF OF AMICUS CURIAE TAX EXECUTIVES INSTITUTE, INC. IN SUPPORT OF PETITIONER

INTEREST OF AMICUS CURIAE

Pursuant to Rule 37 of the Rules of this Court, Tax Executives Institute, Inc. respectfully submits this brief as *amicus curiae* in support of the petition for a writ of certiorari.[1] Tax Executives Institute (hereinafter "TEI" or "the Institute") is a voluntary, non-profit association of corporate and other business executives, managers, and administrators who are responsible for the tax affairs of their employers. TEI was organized in 1944 and has approximately 4,900 members who represent more than 2,400 of the leading corporations in the United States and Canada.

TEI is dedicated to promoting the uniform and equitable enforcement of the tax laws throughout the Nation, to reducing the costs and burdens of administration and compliance to the benefit of both the government and taxpayers, and to vindicating the Commerce Clause and other constitutional rights of all business taxpayers. The members of the Institute represent a cross-section of the business community, and almost without exception, the companies represented by the Institute's membership are engaged in interstate commerce. Thus, substantially all TEI members will be directly affected by the Supreme Court's decision whether to grant a writ of certiorari in this case.

The issue presented in this case is whether the Commerce and Due Process Clauses preclude South Carolina and other States from taxing the income of a corporation whose presence in the state is not physical, but involves only the use of its trademark (or other intangible property) by a licensee. The case raises the question spe-

---

[1] TEI has requested and received the written consents of the Petitioner and the Respondent to the filing of this brief; those consents have been filed with the Clerk of this Court.

cifically reserved by the Supreme Court in *Quill Corp. v. North Dakota*, 112 S. Ct. 1904 (1992): Whether *Quill*'s bright-line nexus test (which requires a physical presence in the State) applies to taxes other than sales and use taxes. It also raises questions about the scope of the Court's holding in *Quill* that the Due Process Clause does not preclude the taxation of a taxpayer who, although not physically present within a State, has "purposefully directed" its activities at the State. Finally, it brings into doubt the effectiveness of Public Law No. 86-272, 73 Stat. 555 (codified at 15 U.S.C. § 381 (1988)), which circumscribes the States' power to tax income derived from interstate sales of tangible personal property, as interpreted by the Court in *Wisconsin Dep't of Revenue v. William Wrigley, Jr., Co.*, 112 S. Ct. 2447 (1992).

Because TEI members and the companies by whom they are employed will be materially affected by the Court's disposition of these issues, the Institute has a special interest in this case.

SUMMARY OF ARGUMENT

The core issue presented by this case is whether the use of Geoffrey, Inc.'s intangible interests by a third party in South Carolina subjected the corporation to income tax in the State. With minimal analysis, the South Carolina Supreme Court answered this question yes. The lower court's holding casts a shadow over the protections accorded interstate businesses by the Constitution.

1. A threshold requirement of the Commerce Clause is the presence of "sufficient nexus" between the State and the person, property, or transaction to be taxed. Absent such a connection, the tax will be struck down as unconstitutional. Two terms ago in *Quill Corp. v. North Dakota*, 112 S. Ct. 1904 (1992), the Court addressed whether the nexus requirements of the Due Process and Commerce Clauses are co-extensive. It found that while "a State may, consistent with the Due Process Clause, have the authority to tax a particular taxpayer, imposition of the tax may nonetheless violate the Commerce Clause." *Id.* at 1909.

Quill effectively harmonized the Court's decision in *Complete Auto Transit v. Brady*, 430 U.S. 274 (1977), with the Court's 1967 decision in *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967), which held that a vendor's physical presence in a State was required before a sales and use tax obligation could be imposed. Even though *Quill* overruled *National Bellas Hess*'s due process holding, it reaffirmed that a vendor whose only contacts with the taxing States are by mail or common carrier lacks the substantial nexus required by the Commerce Clause to be subject to sales and use tax. *Id.* The Court in *Quill* did not explicitly extend its holding beyond the sales and use tax area, but it cautioned that its failure to articulate a physical-presence test in other areas "does not imply repudiation of the [*National*] *Bellas Hess* rule" in those areas. *Id.* at 1914.

2. The court below paid scant attention to the reasoning and mandate of this Court's decision in *Quill*, and did not analyze whether and why income taxes should be treated differently from sales and use taxes.

Amicus TEI submits that they should not: A bright-line, physical-presence test should be adopted to avoid "undue burdens on interstate commerce . . . by the demarcation of a discrete realm of commercial activity that is free from interstate taxation." *Id.* at 1914. Such a test would firmly establish the boundaries of legitimate state authority, reduce litigation, encourage settled expectations, and promote stability and the orderly development of the law. *See id.* at 1915-16. Indeed, ample grounds exist for imposing a *higher* nexus standard in respect of income taxes.

The lower court's analysis resembles that of the lower court in *Quill*, which had argued that an "economic presence" test should be applied. The South Carolina court held that the nexus requirement of the Constitution was satisfied merely by the "presence" of intangible property in South Carolina, making specific reference to Geoffrey's accounts receivable in the State. This chimerical nexus test should be rejected as a one-way street to ration-

alize taxing schemes, not to vindicate the Commerce Clause rights of interstate taxpayers. Moreover, the test propounded by the South Carolina court is unreasonably vague, and would impose undue administrative costs and burdens on interstate business.

Under the South Carolina court's analysis, the sale of any type of property (tangible or intangible) or service on credit could arguably subject an out-of-state seller to income tax, regardless of whether the seller had any presence (physical or otherwise) in the State. The lower court's jurisdictional alchemy would massively expand the obligation of taxpayers to comply with a plethora of state tax filing obligations. It was concerns with such administrative costs and burdens that informed the Court's Commerce Clause analysis in *Quill*, and that led the Court to affirm the vitality of the physical-presence test in respect of sales and use tax. Such concerns, regrettably, were lost on the court below. A writ of certiorari should be issued in this case to remedy that shortcoming and to confirm the application of a bright-line, physical-presence test to income tax cases.

3. In *Quill*, this Court decoupled the constitutional requirement of nexus for Commerce Clause purposes from the nexus requirement for due process purposes. It did not, however, read the Due Process Clause's requirement of nexus out of the Constitution. Rather, it affirmed that a State may subject a foreign corporation to its taxing jurisdiction only if the taxpayer had "minimum contacts" with the jurisdiction.

The South Carolina Supreme Court had little trouble in concluding that the Due Process Clause posed no barrier to the State's assertion of taxing power. The lower court, however, failed to point to any activity of Geoffrey in South Carolina; rather, it focused on activities of its licensee. Clearly, the taxpayer's "contacts" with the State are far less substantial than Quill Corporation's "continuous and widespread solicitation of business within [the] State." *Quill Corp.*, 112 S. Ct. at 1911.

Whereas Quill Corporation's contacts in North Dakota were "more than sufficient" for due process purposes, 112 S. Ct. at 1911, the same cannot be said in respect of Geoffrey's minimal contacts here. The Court should issue a writ of certiorari to vivify the Due Process Clause's limitations on the States' authority to tax.

4. The theory of nexus propounded by the court below is potentially so loose that it could undercut the protections accorded interstate business by Public Law No. 86-272, 73 Stat. 555 (codified at 15 U.S.C. § 381 (1988)), which prohibits the States from taxing the income of a corporation whose only business activities within the State consist of solicitations of orders for sales of tangible personal property. The protections intended by Congress and fortified by the Court two terms ago in *Wisconsin Dep't of Revenue v. William Wrigley, Jr., Co.*, 112 S. Ct. 2447 (1992), however, could well be diluted if the lower court's opinion is allowed to stand.

The court below found the presence of intangible property in South Carolina by virtue of the taxpayer's licensing of trademarks and other intangibles as well as the presence of accounts receivable. If the presence of such "intangible property" were construed to be more than "solicitation" for purposes of Public Law No. 86-272 or to render the law inapplicable, the federal statute would be effectively gutted.

Amicus TEI submits that the Court should issue a writ of certiorari to ensure that the States do not act to frustrate the congressional policy underlying Public Law No. 86-272.

ARGUMENT

The petitioner, Geoffrey, Inc., is the owner of several trade names and trademarks, including "Toys 'R' Us." Geoffrey licensed these trade names and trademarks to Toys "R" Us stores throughout the country, including South Carolina. Under the licensing agreement, Toys "R" Us paid Geoffrey a fee, or royalty, based on total company sales. Geoffrey had no employees, offices, or physical presence within South Carolina, and at the time the licensing agreement was entered into, there were no Toys "R" Us stores located in the State.

The core issue presented by this case is whether the use of Geoffrey's intangible interests in South Carolina subjected the corporation to income tax in the State. With minimal analysis, the South Carolina Supreme Court answered this question yes. It averred that a "taxpayer need not have a tangible, physical presence in a state for income to be taxable" and blithely sought to distinguish this Court's 1992 holding in *Quill Corp. v. North Dakota*, 112 S. Ct. 1904 (1992)—which requires such a physical presence—on the ground that *Quill* involved sales and use taxes (rather than income taxes). App. A at 9a & n.4.[2] The South Carolina court also held that "by licensing intangibles for use in this State and deriving income for their use here, Geoffrey has a 'substantial nexus' with South Carolina." App. A at 10a (footnote omitted).

The holding of the court below casts a long shadow over the protections accorded interstate businesses by both the Commerce and Due Process Clauses of the Constitution.[3] The South Carolina court misapprehended this Court's

---

[2] References to "App." are to the appendix filed with Geoffrey, Inc.'s Petition for a Writ of Certiorari to the Supreme Court of South Carolina (No. 93-520).

[3] U.S. Const. art. I, § 8, cl. 3 (Commerce Clause); U.S. Const. amend. XIV, § 1 (Due Process Clause).

decision in *Quill* in two respects: First, it erroneously concluded that the bright-line, physical-presence test embraced by the Court for Commerce Clause purposes has no application in respect of income taxes. Secondly, it misconstrued the limitations the Due Process Clause imposes on States, notwithstanding this Court's finding that the Due Process Clause's nexus requirement is not coextensive with the Commerce Clause's analogous requirement. Thus, under the lower court's analysis, the States would be free to tax even where taxation would offend "traditional notions of fair play and substantial justice." *See Quill Corp.*, 112 S. Ct. at 1910 (quoting *International Shoe Co. v. Washington*, 326 U.S. 310, 316 (1945)). Moreover, by conjuring nexus between a licensor and the State out of a *licensee*'s use of a trademark, the lower court set forth a standard so amorphous and vague that it could not help but subvert basic Commerce Clause principles. Moreover, to the extent the intangible property is imbedded in tangible property, the decision below undermines the statutory protection afforded interstate businesses by Public Law No. 86-272, 73 Stat. 555 (codified at 15 U.S.C. § 381 (1988)). *See Wisconsin Dep't of Revenue v. William Wrigley, Jr., Co.*, 112 S. Ct. 2447, 2453-54 (1992).

The court should grant a writ of certiorari in order to turn back this effort by the State of South Carolina to vitiate the Court's recent holdings in *Quill* and *Wrigley* and thereby frustrate interstate commerce.

I.

The "fundamental purpose of the [Commerce] Clause is to assure that there be free trade among the several States." *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318, 335 (1977). In tandem with the Due Process Clause of the Fourteenth Amendment, the Commerce Clause acts to prevent the States from enacting unfair

tax or tax collection statutes and thereby imposing "unreasonable clog[s] upon the mobility of commerce." *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935); *see* PAUL J. HARTMAN, FEDERAL LIMITATIONS ON STATE AND LOCAL TAXATION §§ 2.2, 2.1 (1981).

Because the Commerce Clause was intended to protect "the free flow of trade between the States," "[s]tate taxation falling on interstate commerce . . . can only be justified as designed to make such commerce bear a fair share of the cost of the local government whose protection it enjoys." *Freeman v. Hewit*, 329 U.S. 249, 252, 253 (1946). In determining whether a particular state taxing scheme is constitutionally valid, this Court has held that "due process requires some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." *Miller Bros. v. Maryland*, 347 U.S. 340, 344-45 (1954). In *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967), the Court cited *Miller Bros.* with approval and imported its "definite link, some minimum connection"—or nexus—standard into its Commerce Clause analysis. *Id.* at 756, *quoting Miller Bros.*, 347 U.S. at 344-45.

The overarching importance of nexus to Commerce Clause determinations is underscored by the Court's seminal decision in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), and its holding two terms ago in *Quill*. In *Complete Auto Transit*, the Court established a four-prong test for determining whether a state tax statute violates the Commerce Clause, holding that such a tax will be sustained only if (1) it is applied to an activity with a substantial nexus with the taxing State, (2) it is fairly apportioned, (3) it does not discriminate against interstate commerce, and (4) it is fairly related to the services provided by the State. *Id.* at 279. Thus, *Complete Auto Transit* sets forth a decisional framework for Commerce Clause inquiries that requires a balancing of competing interests in determining whether the tax unduly infringes on interstate commerce. *See, e.g., Trinova Corp.*

v. Michigan Dep't of Treasury, 498 U.S. 358, 372-73 (1991); *Exxon Corp. v. Department of Revenue*, 447 U.S. 207, 227-28 (1980).

A threshold requirement of the Commerce Clause is the presence of "sufficient nexus" between the State and the person, property, or transaction to be taxed. Absent such a connection, the "fairness" of the particular levy—measured in terms of whether it is properly apportioned or whether it is reasonably related to the services provided by the State—is irrelevant: The tax will be struck down as unconstitutional. *See Quill Corp.*, 112 S. Ct. at 1909; *Trinova Corp.*, 498 U.S. at 372-73; *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 436-37 (1980). In other words, if the connection, or linkage, is insubstantial or remote, the State has not "given anything for which it can ask return," *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444 (1940), and the State's effort to assert its taxing authority must be turned aside.

Two terms ago in *Quill*, the Court addressed whether the nexus requirements of the Due Process and Commerce Clauses are co-extensive.[4] The Court severed the two standards, explaining that they are "animated by different constitutional concerns and policies":

> [T]he due process nexus analysis requires that we ask whether an individual's connections with a State are substantial enough to legitimate the State's exercise of power over him. . . . In contrast, the Commerce Clause, and its nexus requirement, are informed not so much by concerns about fairness for the individual defendants as by structural concerns

---

[4] The Court elaborated that "'[t]here may be more than sufficient factual connections, with economic and legal effects, between the transaction and the taxing state to sustain the tax as against due process objections. Yet it may fall because of its burdening effect upon the commerce.'" 112 S. Ct. at 1909 (quoting *International Harvester Co. v. Department of Treasury*, 322 U.S. 340, 353 (1944) (Rutledge, J., concurring in part and dissenting in part)).

about the effects of state regulation on the national economy.

112 S. Ct. at 1913.[5]

Quill confirmed the vitality of the *Complete Auto Transit* construct and effectively harmonized that decision with the Court's 1967 decision in *National Bellas Hess*, which had held that a sales and use tax could not constitutionally be imposed on a vendor whose only contacts with the taxing State are by mail or common carrier.[6] It also reaffirmed the constitutional prerequisite (for Commerce Clause purposes) of the taxpayer's physical presence in the taxing jurisdiction, though it overruled *National Bellas Hess*'s due process holding. *Quill Corp.*, 112 S. Ct. at 1916. Thus, *Quill* confirmed that a vendor whose only contacts with the taxing State are by mail or common-carrier lacks the substantial nexus required by the Commerce Clause. *Id.* The Court embraced *National Bellas Hess*'s bright-line, physical-presence test of Commerce Clause nexus not only because such a test "furthers the ends of the dormant Commerce Clause" by "demar-

---

[5] Thus, "a State may, consistent with the Due Process Clause, have the authority to tax a particular taxpayer, [while] imposition of the tax may nonetheless violate the Commerce Clause." *Id.*, at 1909 (citing *Tyler Pipe Industries, Inc. v. Washington State Dep't of Revenue*, 483 U.S. 232 (1987)). In differentiating the two standards, the Court in *Quill* noted that "the 'substantial-nexus' requirement is not, like due process' 'minimum-contacts' requirement, a proxy for notice, but rather a means for limiting state burdens on interstate commerce." 112 S. Ct. at 1913.

[6] In *National Bellas Hess*, the Court struck down Illinois's effort to require an out-of-state mail-order business to collect the use tax on mail-order sales made to state residents on both due process and Commerce Clause grounds. The Court explained that sanctioning the imposition of a use tax collection duty on a business that maintained no physical presence in the State would give rise to "unjustifiable local entanglements" of interstate commerce. 386 U.S. at 760. The Court reasoned that the administrative and record-keeping requirements that could arise in the absence of a physical presence test "could entangle National [Bellas Hess]'s interstate business in a virtual welter of complicated obligations to local jurisdictions . . . ." *Id.* at 759-60.

cati[ng] . . . a discrete realm of commercial activity that is free from interstate taxation," *id.* at 1914, but because it fosters the "interest in stability and orderly development of the law" that undergirds the doctrine of *start decisis*. *Runyon v. McCrary*, 427 U.S. 160, 190-91 (1976) (Stevens, J., concurring) (quoted in *Quill Corp.*, 112 S. Ct. at 1916).[7] The Court in *Quill* did not explicitly extend its holding beyond the sales and use tax area, but it cautioned that its failure to articulate a physical-presence test in other areas "does not imply repudiation of the [*National*] *Bellas Hess* rule" in those areas. *Id.* at 1914.

II.

The court below paid scant attention to the reasoning and mandate of the decision in *Quill*. Rather, it embarked on a results-oriented journey very similar to the North Dakota trip that the Court in *Quill* found to contravene the Commerce Clause. Holding that "[t]he presence of intangible property alone is sufficient to establish nexus," App. A at 9a, the South Carolina court dismissed *Quill* with a wave of its hand, noting only that this Court had observed that, to date, the physical-presence test had not been extended beyond the sales and use tax area. App. A at 9a n.4. Thus, the lower court gave no weight to the statement in *Quill* that the failure to articulate a physical-presence test in other areas "does not imply repudiation of the [*National*] *Bellas Hess* rule" in respect of income taxes. 112 S. Ct. at 1914. More to the point, it did not analyze whether and why income taxes should be treated differently from sales and use taxes.

Amicus TEI submits that they should not: A bright-line, physical-presence test should be adopted to avoid "[u]ndue burdens on interstate commerce . . . by the demarcation of a discrete realm of commercial activity that is free from interstate taxation." *Id.* at 1914. Such a test

---

[7] "[T]he continuing value of a bright-line rule in this area and the doctrine and principles of *stare decisis* indicate the [*National*] *Bellas Hess* rule remains good law." *Quill Corp.*, 112 S. Ct. at 1916.

would firmly establish the boundaries of legitimate state authority, reduce litigation, encourage settled expectations, and promote stability and the orderly development of the law. *See id.* at 1915-16.

Indeed, ample grounds exist for concluding that the nexus requirement for income tax purposes is *more* demanding than the requirement for sales and use tax purposes. Unlike sales and use taxes, which are transaction-based, the authority to impose an income tax is predicated on a taxpayer's own links to the taxing jurisdiction—that is to say, whether the taxpayer is sufficiently present, or active, in the State (and derives sufficient benefits from the State) to satisfy the Constitution's minimum contacts requirement. The transactions being taxed under a sales and use taxing scheme are themselves a link between the taxpayer and the State, a connection that must be buttressed by the taxpayer's physical presence in order to survive constitutional scrutiny. Where the tax is imposed not on transactions but on income, an even-more-substantial connection should be required.[8]

The need for as high or even a higher standard of constitutional nexus for income tax purposes is underscored by Congress's enactment of Public Law No. 86-272, which prohibits States from taxing income derived from interstate sales of tangible personal property if the only activities of the out-of-state person within the State are the solicitation of orders. Although the prohibition in Public Law No. 86-272 is not absolute, the legislation does evidence Congress's intent to erect a higher barrier to state *income* taxation to ensure that the States' taxing schemes do not unduly impede interstate commerce. Ratification of, or acquiescence in, the lower court's analysis would so impede interstate commerce.[9]

---

[8] Thus, it is not at all uncommon for taxpayers to pay sales and use taxes (on a transactional basis) in more jurisdictions than those in which they are required to register and pay income taxes.

[9] For a further discussion of Public Law No. 86-272, see part IV of the Argument.

That the bright-line test of *Quill* should be extended to the income tax area is made manifest by what the lower court did in the absence of such a test. The court held that the nexus requirement was satisfied merely by the "presence" of "intangible property" in South Carolina, making specific reference to Geoffrey's accounts receivable (for licensing fees) created on the sales by the licensee, App. A at 5a, as well as to the "franchise" the court held was created by the agreement that permitted the licensee to sell a product or service under a trademark or trade name owned by the licensor. App. A at 5a & n.2. The court's analysis thus resembles that of the lower court in *Quill*, which had spuriously argued that a makeweight "economic presence" test should suffice for Commerce Clause purposes.

If such a standard (however denominated) were to come into force, however, the Commerce Clause rights of interstate business as a whole would be jeopardized for two reasons: First, intangible property rights are so prevalent in today's economy that the test would give States a sweeping license to tax broad classes of businesses without regard to whether they have, as a practical matter, substantial contacts with, or economic activity in, the taxing jurisdiction. In other words, this chimerical nexus test would operate as a one-way street to rationalize taxing schemes, not to vindicate the Commerce Clause rights of interstate taxpayers. Secondly, the test propounded by the South Carolina court is at once both unreasonably vague and unacceptably broad, and would impose undue administrative costs and burdens on interstate business.

The South Carolina Supreme Court would apply what might be called the Willie Sutton test of constitutional adjudication: *Why does the State assert that it has sufficient nexus to impose an income tax on Geoffrey? Because Geoffrey is where the money is.* Thus, in defending its finding of nexus, the court baldly stated:

> That Geoffrey has received protection, benefits, and opportunities from South Carolina [sufficient to jus-

> tify a finding of nexus] is manifested by the fact that it earns income in this state.

App. A at 9a. In other words, because there is income to be taxed, it must be taxable by the State of South Carolina. Surely this tautology cannot pass constitutional muster.

To be sure, the lower court identified "intangible property" within the State that it said justified its conclusion, but in point of fact Geoffrey itself engaged in no business activity within South Carolina. More fundamentally, the lower court's standard is so broad that it would sweep an extraordinary amount of out-of-state businesses within its taxing net. Consider what would give rise to tax and who would be taxable under the lower court's analysis. Every sale of a Mickey Mouse T-shirt or a personal computer with MS-DOS and Windows installed and "Intel inside" would give rise to a royalty or licensing fee subject to tax. Indeed, whenever one person's intangible property (be it a copyright, trademark, trade name, patent, or some similar property) was used by others, the person would be subject to tax where the property was used—regardless of whether the person had any say in the matter—and to the attendant filing and compliance costs.

Movie stars who receive a percentage of ticket sales would be taxable in every jurisdiction in which their films are shown. A musician who receives a royalty on the sale of records or compact disks would be subject to tax in every State in which a sale is made, as would authors whose publishing contracts call for a per-book royalty.[10] Hence, pop singer Phil Collins would be subject to tax in each State in which a copy of his recording "In the Air Tonight" is sold and mystery writer Mary Stewart would find herself subject to tax in each State in which a reader buys *Airs Above the Ground*—an ironic result

---

[10] Query whether authors receiving payments from the Copyright Clearance Center in respect of copies of articles published in academic journals (and elsewhere) would find themselves subject to tax in those jurisdictions from which the payments were made.

perhaps inasmuch as the States would seem to be conjuring nexus out of thin air.[11]

South Carolina's concept of nexus is further distended by the lower court's intimation that accounts receivable constitute intangible property sufficient to support the State's assertion of taxing power. App. A at 5a-6a. Hence, the sale of any type of property (tangible or intangible) or service on credit could arguably subject an out-of-state seller to income tax, regardless of whether the seller had any presence in the State. Such an expansive, ethereal definition of nexus would leave the States free to wield "intangible property" as a shibboleth to eviscerate the protections of the Commerce Clause. In other words, the nexus requirement as interpreted by the lower court would become little more than the word "glory" in *Through the Looking Glass:* meaning whatever the States, like Humpty Dumpty, says it means.[12]

The lower court's jurisdictional alchemy would massively expand the obligation of taxpayers to comply with a plethora of state tax filing obligations. Businesses that received income from other persons' use of their intangible property would have to monitor where such property was used, determine what part of the income derived from such use was attributable to which jurisdiction, research the tax consequences of such use in each jurisdiction, and then undertake to comply. They would likely have to revise their licensing agreements, change their accounting systems to capture the necessary information, and set in

---

[11] In *Quill*, this Court found that Quill Corporation's licensing of software to some North Dakota customers did not satisfy the Commerce Clause's "substantial nexus" requirement. 112 S. Ct. at 1914 n.8. The Court confirmed that more than a "slightest presence" standard—such as it rejected in *National Geographic Society v. California Bd. of Equalization*, 430 U.S. 551, 556 (1977)—is required under the Constitution. 112 S. Ct. at 1914 n.8.

[12] LEWIS CARROLL, THROUGH THE LOOKING GLASS 186 (Signet Classic 1960) ("'When *I* use a word ['glory'],' Humpty Dumpty said, in a rather scornful tone, 'it means just what I choose it to mean—neither more nor less.'").

place procedures to ensure compliance with myriad filing and reporting requirements. None of these tasks would be easy, and none would be cheap. The burden of uncertainty, exacerbated by the cost of good faith compliance efforts, could not help but act as an "unreasonable clog upon the mobility of commerce." *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. at 527.

It was concerns with administrative costs and burdens that informed the Court's Commerce Clause analysis in *Quill*, and such concerns that led the Court to affirm the vitality of the physical-presence test in respect of sales and use tax. Such concerns, regrettably, were lost on the court below. A writ of certiorari should be issued to remedy that shortcoming by confirming the application of a bright-line, physical-presence test to income tax cases.

III.

In *Quill*, this Court decoupled the constitutional requirement of nexus for Commerce Clause purposes from the nexus requirement for due process purposes. Even though the Court held that due process jurisprudence had evolved beyond an absolute prerequisite of physical presence, it did not read the Due Process Clause's requirement of nexus out of the Constitution. Rather, it affirmed that a State may subject a foreign corporation to its taxing jurisdiction only if the taxpayer had "minimum contacts with the jurisdiction" to ensure against offending "traditional notions of fair play and substantial justice." 112 S. Ct. at 1910 (quoting *International Shoe Co.*, 326 U.S. at 316); *accord Milliken v. Meyer*, 311 U.S. 457, 463 (1940).[13]

---

[13] In other words, the due process nexus requirement was not rendered a nullity; a taxpayer's "purposefully avail[ing] itself of the benefits of an economic market in the forum State" and "purposefully direct[ing]" its activities at residents of that State are simply now to be considered in determining whether the assertion of jurisdiction would comport with "fair play and substantial justice." 112 S. Ct. at 1910, 1911 (citing *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 476 (1985)); *see International Shoe*, 326 U.S. at 320.

The South Carolina Supreme Court had little trouble concluding that the Due Process Clause posed no barrier to the State's assertion of taxing power over Geoffrey. It reached this conclusion, however, by turning the "purposefully directed" test on its head. Specifically, the lower court did not point to any activity of Geoffrey in South Carolina, but rather to activities of its licensee. It then averred that "Geoffrey had not been unwillingly brought into contact with South Carolina through the unilateral activity of an independent party." App. A at 5a. Clearly, however, Geoffrey's "contacts" with South Carolina are far less substantial than Quill Corporation's "continuous and widespread solicitation of business" within North Dakota. 112 S. Ct. at 1911. More fundamentally, the Court in *Quill* observed that a company engaging in such extensive solicitations "has 'fair warning that [its] activity may subject [it] to the jurisdiction of a foreign sovereign.'" *Id.* at 1911 (quoting *Shaffer v. Heitner*, 433 U.S. 186, 218 (1977) (Stevens, J., concurring) (brackets in original)). Where was the warning here?

Thus, whereas Quill Corporation's contacts in North Dakota were "more than sufficient" for due process purposes, 112 S. Ct. at 1911, the same cannot be said in respect of Geoffrey's contacts here. Indeed, the lower court ignored the second prong of the Court's due process analysis: whether the assertion of taxing jurisdiction comports with traditional notions of fair play and substantial justice. This may not be surprising given Geoffrey's attenuated connection with the State, but neither should it stand. *Amicus* TEI urges the Court to issue a writ of certiorari to vivify the Due Process Clause's limitations on the States' authority to tax.

IV.

The theory of nexus propounded by the court below is so open-ended that it could significantly undercut the protections accorded interstate business by Public Law No. 86-272. That law, which was enacted by Congress in

1959 in furtherance of its responsibility to regulate interstate commerce, prohibits the States from taxing the income of a corporation whose only business activities within the State consist of "solicitations of orders . . . for sales of tangible personal property," where the orders are sent outside the State for approval and the goods are delivered from out-of-state. *Id.*; *see Wrigley*, 112 S. Ct. at 2450. The legislation, however, does not extend to sales of services or intangible property.

Two terms ago, the Court in *Wrigley* brought considerable clarity to Public Law No. 86-272 by interpreting the term "solicitation." The protections intended by Congress and fortified by the Court in *Wrigley*, however, could well be diluted if the lower court's opinion is allowed to stand. As previously stated, the court found the presence of intangible property in South Carolina by virtue of the taxpayer's licensing of trademarks and other intangibles as well as the presence of accounts receivable in respect of sales by the licensee. If the presence of such "intangible property" in the State were construed to be more than "solicitation" for purposes of Public Law No. 86-272, the federal statute would be effectively gutted. Similarly, where the sale of tangible personal property (otherwise falling within the ambit of Public Law No. 86-272) is bundled with a license to use intangible property (*e.g.*, a trademark, copyright, or patent)—as is quite common—the lower court's analysis could rob taxpayers of the protection of the statute, even though they hew closely to the guidelines set forth in *Wrigley*.

Consider the case of the manufacturer whose sales of tangible personal property are shielded from state income taxation on the grounds that its activities in the State do not extend beyond mere solicitation. If the property is stamped with the manufacturer's trademark, would a State be free, notwithstanding Public Law No. 86-272, to impose its income tax on the manufacturer on the basis of the use of the imbedded intangible property in the

State?[14] In the absence of guidance from the Court, the States may well act to frustrate the congressional policy undergirding Public Law No. 86-272.[15]

The potential dissonance among the Court's teaching in *Quill*, the Commerce Clause's nexus requirement for income tax purposes, and the scope of the federal statute —should the lower court's opinion stand—is illustrated by the following example.

> A musician writes, copyrights, and records several songs and regularly advertises their sale on cassette tapes through a national cable television station. Orders are received from residents of several States who pay by credit card, and the tapes are shipped through the mail or by common carrier. Under *Quill*, the musician is not obliged to collect the market States' use tax because the musician has no physical contacts with those States, other than through the mail or by common carrier. If the lower court's analysis applies for income tax purposes, however, the States could well assert jurisdiction to tax. Specifically, they could claim that Public Law No. 86-272 does not preclude their imposition of income tax because intangible personal property—the copyrighted music—was sold in addition to the tangible tapes.[16]

---

[14] The merchandise subject to the Court's attention in *Wrigley*—chewing gum—clearly had intangibles (*e.g.*, the trade names Juicy Fruit and Doublemint) associated with it.

[15] There is evidence the States are poised to act. *See, e.g.*, Robert M. Fahrenbach, *DOR to Monitor* Geoffrey *Case, Intercompany Transactions*, 5 STATE TAX NOTES, July 26, 1993, at 300 (Wisconsin); William D. Townsend, *Revenue Department Drafts Substantial Rewrite of Corporate Income Tax Rules*, 5 STATE TAX NOTES, July 5, 1993, at 7 (Florida). *See generally* Federation of Tax Administrators, *South Carolina High Court Applies* Quill *Decision*, 57 TAX ADMINISTRATORS NEWS 69, 80 (July 1993) (the *Geoffrey* case "could become a basis for other state courts to hold companies subject to income and franchise taxes on the basis of economic presence").

[16] This illustration is based on an example set forth in Jeffrey S. Peters, *Commentary: Income Tax Nexus—Geoffrey Raises New Questions after Quill*, OHIO TAX SERV. 9-11, 9-12 (Dec. 1992).

Amicus TEI submits that the Court should issue a writ of certiorari and ensure that such a result will not obtain.

CONCLUSION

For the foregoing reasons, the Court should grant a writ of certiorari in this case.

Respectfully submitted,

TIMOTHY J. MCCORMALLY
Counsel of Record
MARY L. FAHEY
TAX EXECUTIVES INSTITUTE, INC.
1001 Pennsylvania Avenue, N.W.
Suite 320
Washington, D.C. 20004-2505
(202) 638-5601
Counsel for Amicus Curiae
Tax Executives Institute, Inc.

November 1, 1993